United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

To be Argued By
Jacob D. Zeldes

76-5025

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In the Matter Of The New York, New Haven
and Hartford Railroad Company, Debtor

B
P/S

LAWRENCE W. IANNOTTI, Successor Indenture Trustee Under The New York, New Haven And Hartford Railroad Company's First And Refunding Mortgage Dated As Of July 1, 1947; and

JACOB D. ZELDES, Successor Indenture Trustee Under The New York, New Haven And Hartford Railroad Company's General Income Mortgage Dated As Of July 1, 1947,

Appellants,

v.

MANUFACTURERS HANOVER TRUST COMPANY, Former Indenture Trustee Under The New York, New Haven And Hartford Railroad Company's First And Refunding Mortgage Dated As Of July 1, 1947; and

RICHARD JOYCE SMITH, Trustee Of The Property Of The New York, New Haven And Hartford Railroad Company, Debtor,

Appellees.

On Appeal From The United States District Court For The District Of Connecticut, Honorable Robert P. Anderson, Circuit Judge, Sitting By Designation

REPLY BRIEF OF SUCCESSOR INDENTURE TRUSTEES

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IN THE UNITED STATES COURT OF APPEALS
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In the Matter of The New York, New Haven and Hartford Railroad Company, Debtor

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REPLY BRIEF OF SUCCESSOR INDENTURE TRUSTEES

Manufacturers, in the precise words of the Reorganization Court judge who has supervised this proceeding since its inception 16 years ago

> "has 'pursued [an] interest adverse to the New Haven estate' in pursuing the interests of the 18 New York Central and/or Pennsylvania Railroad indentures...

> "...it is clear that the breach of fiduciary duty by Manufacturers Hanover to the New Haven's first mortgage bondholders has impeded, and therefore damaged, the New Haven reorganization trustee's collection of the sums owed the New Haven estate from the Penn Central for the transferred properties of the New Haven and has frustrated the further development of a plan of reorganization for the New Haven..." (A513-514) (Emphasis added).

When we argue that Manufacturers should be denied payment for itself and its counsel from the estate with which it is in conflict on the central issue remaining in the reorganization, Manufacturers labels the argument as one calling for a "drastic penalty" which has the effect of "robbing" Manufacturers and its counsel and is "so obnoxious to equitable principles" (Manu. Br. 19).[1] Such alarm is hardly consistent with Manufacturers' past actions. From the outset of its participation in the New Haven reorganization, Manufacturers was well aware that as an indenture trustee it could not, as a matter of law, serve conflicting interests, and that, if it did, its right, as well as the right of its counsel, to obtain compensation for services rendered and reimbursement of expenses from the debtor's estate would most certainly be adversely affected. In its original petition to intervene in the New Haven reorganization proceedings, Manufacturers requested the New Haven Reorganization Court to find, and it so found, that the facts and activities set forth in their petition

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1. References to the Brief of Appellants are designated "(Br.)"; references to the Brief of Appellee Manufacturers Hanover Trust Company are designated "(Manu. Br.)"; references to the Brief of Appellee the New Haven Trustee are designated "(Smith Br.)"; and references to the numbered pages of the Joint Appendix are designated "(A)".

"do not constitute a conflict of interest on the part of the petitioners which would make it inappropriate for them to participate in this proceeding on behalf of the holders of the Debtor's First and Refunding Mortgage Bonds or which would affect their right, and the right of their counsel, hereinafter to make application to the Court and obtain compensation for services rendered and reimbursement of expenses incurred in connection with or during this proceeding;..." (Emphasis added.)[2]

Notwithstanding recognition ab initio that its right and its counsel's right to "'reasonable compensation for services rendered' necessarily implies loyal and disinterested service in the interest of those for whom the claimant purported to act," Woods v. City National Bank and Trust Company of Chicago, 312 U.S. 262, 268 (1941), Manufacturers asks this Court to uphold a potential award of $1,535,568.83 out of the New Haven estate, while it continues to occupy fiduciary positions in conflict with the New Haven estate on the central issue involved in the reorganization.

By way of response, appellant Successor Indenture Trustees reply in three parts: first, we point out that many of the factual assertions upon which Manufacturers bases its legal argument are inconsistent with the record or the precise findings of the Reorganization Court; second, we point out that Woods' strict rule of denying compensation to fiduciaries with conflicting interests is based on--

2. This language appears both in the Petition of Manufacturers Trust Company, Corporate Trustee, and A. Frederick Keuthen, Successor Individual Trustee, Under A First And Refunding Mortgage Dated As Of July 1, 1947 of the New York, New Haven and Hartford Railroad Company for Permission to Intervene dated July 25, 1961, at pp. 9-10, and in Judge Anderson's order, dated September 6, 1961, granting the petition. Although neither document appears in the Joint Appendix, both are included in the Sixth Supplement to the Record on Appeal (Docs. 1, 4). For the convenience of the Court, a copy of the order is attached to this brief.

not contrary to--basic equitable principles; and third, we comment briefly on the Reorganization trustee's change of attitude toward Manufacturers' conflict of interest.

I. MANUFACTURERS' FACTUAL ASSERTIONS AND THE STATUS OF THE RECORD.

A.

Argues Manufacturers: Manufacturers, in July, 1970, advised the New Haven Reorganization Court as well as the Penn Central Reorganization Court of its conflict of interests (Manu. Br. 6, 16, 18 n. 16).[3]

The record demonstrates: Examination of Manufacturers vice-president discloses:

> "Q. [By Professor Moore:] Mr. Byrne, were you advised whether or not you could petition Judge Anderson and Judge Fullam to have special counsel or special trustee appointed?
>
> "MR. BADER: Could I hear the question?

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3. Manufacturers' repeated assertions that in July, 1970 Manufacturers, through its counsel, advised the New Haven Reorganization Court as well as the Penn Central Reorganization Court of its conflict of interests (Manu. Br. 6, 16, 18 n. 16), are supported solely by counsel's affidavit which merely notes some informal discussions. Significantly, the citations in Manufacturers' brief to support its claim that it advised the New Haven Reorganization Court are references to counsel's affidavit in support of Manufacturers' petition for compensation dated June 12, 1975, almost five years after the conflict arose. In any event, that affidavit merely notes some informal discussion among various counsel concerning Manufacturers' conflicts and counsel's claimed informal discussion with Judge Anderson (A221). Significantly, the citations in support of its claim that it informed the Penn Central Reorganization Court of its conflicts are references to the reply brief which Manufacturers filed in the court below (A322 et seq.)--a document equally devoid of references to anything in the record of these proceedings which supports these factual assertions. For obvious reasons Manufacturers never claimed to the New Haven Reorganization Court that it had advised that court of its conflicting interests. And, as noted, Manufacturers knew a more proper way to bring the potential conflict to the court's attention: It had done just that in its petition to intervene.

(The previous question was read back by the Reporter.)

"MR. BADER: Could we fix this as to time?

"PROFESSOR MOORE: Any time.

"MR. BADER: Well, I think the only real issue is between July 1 and August 10, and I don't think it would have been feasible then -- I think it's pertinent what time we are talking about.

"THE COURT: Well, I think it's a proper question as far as any time after the Penn Central went into bankruptcy. From then to the present. At any time there was no petition to me that I recollect with regard to them.

"THE WITNESS: No, sir.

"THE COURT: And, of course, I would have no authority over them because they're all New York Central bonds, and I take it that would come before Judge Fullam in the Eastern District of Pennsylvania.

"THE WITNESS: And I answer your question no.

"THE COURT: Was a petition made to him relative to the appointment of substitute trustee --

"THE WITNESS: No, sir.

"THE COURT: -- special master or anything of that sort to fill in where you felt you should resign or at least your Chairman of the Board should decide?

"THE WITNESS: No special, no.

"THE COURT: Was anything done outside of the contacting the 62 banks with a view to asking them to step in as indenture trustee? Was anything else done?

"THE WITNESS: No. There wasn't.

"THE COURT: You didn't take the issue up with the Court at all?

"THE WITNESS: No.

"THE COURT: When you found they wouldn't take it, you couldn't find any bank to take it, you just kept on going? I mean the Manufacturers are still acting as indenture trustee --

"THE WITNESS: Yes.

"THE COURT: -- for those bonds?

"THE WITNESS: Yes." (A388-389)(Emphasis added).[4]

B.

Argues Manufacturers: Manufacturers made "efforts to resign its Central trusteeships" (Manu. Br. 8).

The record demonstrates: Judge Anderson specifically found:

"The Trust Company, as indenture trustee for the New York Central and/or Pennsylvania Railroad indentures did speak of resigning but was dissuaded from doing so. It never took a strong stand for that proposition and never, when contemplating its dilemma, refused to serve, following this stand by pressing for or seeking an authoritative court declaration of its rights and duties, as it should have done." (A513)

"The petitioner plainly breached its fiduciary duty to the New Haven Railroad in reorganization and for five years has continued to do so. It has expressly stated its intention to adhere to this position in the future and to oppose and contest the claim of the New Haven estate in reorganization that the purchase price due for the New Haven's property, based upon the Supreme Court's judgment against the Penn Central in the Inclusion Cases, is secured by an equitable lien. For the past three years, at least, the petitioner has made no genuine effort to resign as Indenture Trustees for the remaining 17 bond issues for which it is still Indenture Trustee." (A576)(Emphasis added).

4. The testimony of Manufacturers' Vice President Byrne, the only witness presented for cross-examination by Manufacturers to justify its petition for payment (A367-399), received no comment in Manufacturers' brief in this Court; not a single reference was made to this testimony in Manufacturers' brief here.

C.

Argues Manufacturers: The prediction of the Successor Indenture Trustees that

> "had Manufacturers sought instructions from Judge Anderson in 1970, it would have been told to quit both the New Haven Trusteeship and the Penn Central Trusteeships" is "obviously sheer speculation" (Manu. Br. 16).

The record demonstrates: Judge Anderson specifically stated:

> "Manufacturers Hanover should have resigned from both, as its Chairman had said, but apparently no one felt the necessity of following through on his admonition." (A512).

D.

Argues Manufacturers:

> "All of these questions [relating to the equitable lien and constructive trust] were handled exclusively by counsel." (Manu. Br. 11).

The record demonstrates: Manufacturers' Vice-President testifying in the Court below stated:

> "Also involved were novel points of law, evidence and valuation theories which had to be considered. Because of all this, it required very close collaboration with counsel and review of comprehensive data throughout the whole proceeding." (A370) (Emphasis added).

And the affidavit of the Senior Vice-President of Manufacturers in support of its petition for compensation states:

> "The matter of the consideration to be received by the Debtor's estate was the subject of numerous meetings among counsel and various officers of the Petitioner which led to court proceedings which eventually involved appeals through the judicial system up to and including the Supreme Court. Meetings with counsel intensified with the filing of a petition in bankruptcy by Penn Central Transportation Company in June of 1970." (A148)(Emphasis added).

E.

Argues Manufacturers: It would have been impractical to resign from both the New Haven and Penn Central indentures (Manu. Br. 8, 16).

The record demonstrates: Judge Anderson considered this and concluded:

> "Nevertheless the prospect of more problems superimposed upon already existing ones of immense difficulty cannot operate to condone a breach of fiduciary duty or justify it." (A511).[5]

5. The Successor Trustees concede, as Manufacturers claims (Manu. Br. 10), that they were inaccurate in claiming that Manufacturers as Indenture Trustee in the New Haven estate participated in the appeal to this Court in In re New York, New Haven and Hartford Railroad Co., 457 F.2d 683 (2 Cir.), cert. denied, 409 U.S. 890 (1972). Manufacturers did, however, participate in that appeal in its capacity as indenture trustee of the Penn Central mortgages and was in a position hostile to the interests of the New Haven estate.

II. THE WOODS RULE AND THE PRINCIPLES OF EQUITY.

Manufacturers states as its basic tenet,[6] as indeed it must to permit the challenged order to stand, that

> "Woods recognizes and affirms the inherent discretionary authority of a reorganization court to allow or disallow compensation for services and reimbursement for expenses of trustees, having due regard for individual circumstances." (Manu. Br. 20).

> "The Supreme Court held in Woods...that a bankruptcy court might, in its discretion, deny compensation to a fiduciary who has breached his fiduciary duties..." (Manu. Br. 20).

For these two interpretations, Manufacturers makes no reference to the Woods decision (Manu. Br. 20). Indeed it cannot for, contrary to Manufacturers' suggestion, Woods adopted a strict rule of denying compensation to fiduciaries serving conflicting interests. The Court specifically stated that such a fiduciary "should be denied compensation." 312 U.S. at 268.[7]

In attempting to convince this Court that what the Successor Trustees urge is "obnoxious to equitable principles" (Manu. Br. 19),

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6. Faced with Judge Anderson's finding that Manufacturers pursued an interest adverse to the New Haven estate (A513), Manufacturers has abandoned its bold assertion in the lower court that it "'never pursued any interest adverse to the estate.'" (A513), but seems to argue instead that pursuing that adverse interest didn't amount to a breach of trust (Manu. Br. 16).

7. The inflexibility of the Woods rule regarding compensation is manifest from the Supreme Court's relaxation of the rule to allow discretion solely with respect to the reimbursement of the fiduciary's costs and expenses. As the Supreme Court noted,

> "The rule disallowing compensation because of conflicting interests may be equally effective to bar recovery of the expenditures made by a claimant subject to conflicting interests." 312 U.S. at 269.

Manufacturers argues that "the Section 249 cases are inapposite and, therefore, Appellants' 'Woods-Wolf' synthetic theory must fail" (Manu. Br. 25). Manufacturers' argument seems to be that §249 is an anomaly "which overrode the traditional discretion of the court in a single specific context" (Manu. Br. 20), in that it sets much stricter standards for those within its purview than equitable principles otherwise impose. But, as one commentator, cited by the Supreme Court in Wolf v. Weinstein, 372 U.S. 633, 642, n. 10 (1963), has noted, to reach its "strict rule" that a fiduciary serving conflicting interests may not receive compensation for services regardless of his good faith, the Woods court

> "did not rely on any specific provision of the Bankruptcy Act...; instead, the decision was based on the equity powers of bankruptcy courts." Note, Conflict of Interests as a Factor in the Allowance of Representatives' Claims in Insolvent Corporate Reorganizations, 106 U. of Pa. L. Rev. 1139, 1143 (1958)(Emphasis added).

And, as the Supreme Court explained in Wolf, the Congressional purpose behind §249 was "to codify the rule" of federal decisions denying compensation to persons holding fiduciary positions in reorganization proceedings who had traded in the debtor's stock and "to give pervasive effect in Chapter X proceedings to the historic maxim of equity that a fiduciary may not receive compensation for services tainted by disloyalty or conflict of interest." 372 U.S. at 641 (Emphasis added). It is apparent, therefore, that the Supreme Court in Wolf considered the admittedly harsh provisions of §249 to be reflective of the equitable principles announced in Woods--not, as Manufacturers would have it, to be "obnoxious to equitable principles."

Manufacturers claims that Woods and Wolf are "unrelated and cannot be homogenized" (Manu. Br. 20). But the Supreme Court had no trouble whatsoever homogenizing the equitable principles of Woods in reaching its decision in Wolf:

> "Indeed, we have several times declared that the general statutory authorization in the Bankruptcy Act for 'reasonable' compensation for services 'necessarily implies loyal and disinterested service in the interest of those for whom the claimant purported to act.' Woods v. City Nat. Bank & T. Co. 312 U.S. 262, 268, see also American United Mut. L. Ins. Co. v. Avon Park, 311 U.S. 138." 372 U.S. at 642.

The holding in Wolf was not that §249 imposes a harsher penalty on certain fiduciaries than do general equitable principles; rather, it was "that §249 was meant to broaden the classes of fiduciaries to be subjected to [the] traditional sanction" of exclusion from compensation and reimbursement. 372 U.S. at 645. As the Court explained:

> "It should be unnecessary to add that such sanctions are imposed not as penalties, upon the trading itself--for other principles govern the extent to which and conditions under which an insider may profit from investment in the Debtor's securities during the proceeding. Rather, the rationale underlying the denial of compensation and expenses is that allowances may be made, under general equitable limitations and the statutory provisions alike, only for 'loyal and disinterested service in the interest of those for whom the claimant purported to act.' Woods v. City Nat. Bank & T. Co., supra (312 U.S. at 268). Section 249 does no more than declare that one who invests in the Debtor's stock during a reorganization ceases to be disinterested for purposes of compensation and allowances." 372 U.S. at 653, n. 20 (Emphasis added).

Just as the Wolf insider "ceases to be disinterested for purposes of compensation and allowances," the present fiduciary, by virtue of advocating hostile claims, ceases to be "disinterested for purposes

of compensation and allowances." 372 U.S. at 653, n. 20. Since Manufacturers does not qualify as a fiduciary which has rendered "only" loyal and disinterested service, 372 U.S. at 653, n. 20, it must be denied compensation

> "for all services [it] has rendered to the Debtor, however valuable those services may have been... since the start of the reorganization." 372 U.S. at 654.[8]

8. The cases which led the Reorganization Court to disregard the Woods rule--two cases from this Circuit, Berner v. Equitable Office Building Corp., 175 F.2d 218 (2 Cir. 1949), and Silbiger v. Prudence Bonds Corp., 180 F.2d 917 (2 Cir.), cert. denied, 340 U.S. 813 (1950), and one Seventh Circuit case, Chicago West Towns Rys. v. Friedman, 230 F.2d 364 (7 Cir.), cert. denied 351 U.S. 943 (1956) which merely cited Berner and Silbiger to support its "penalty of less than full forfeiture," 230 F.2d at 369--predated Wolf, and must therefore be read with some reservation.

One commentator has noted about Silbiger:

> "The Woods case seemed to establish an acceptable and desirable sanction for the control of committee conduct in corporate reorganization proceedings; however, it was apparently ignored by Judge Learned Hand in deciding Silbiger v. Prudence Bonds Corp.
>
> "* * *
>
> "Although it might be argued that the Woods case and the Silbiger case are so clearly distinguishable by their facts that they are not necessarily inconsistent, it is submitted that, because of the underlying theory of the Supreme Court in the former case, the two cases reach opposite results. The Woods case, in establishing a prophylactic rule, seems to compel complete denial so long as the relationship of dual representation of persons with adverse interests is present. Neither the good faith of the representative in entering into the proceeding nor any beneficial results which might have accrued as a result of his participation are considered by the court under this theory.
>
> "* * *
>
> "It would seem that, assuming some sanction is desirable to prevent the representation of conflicting interests in reorganization proceedings, the Woods case reaches the better result". Note, supra, 106 U. of Pa. L. Rev. at 1144-1147.

As if to justify or excuse the fact that it "impeded" and "frustrated" the Reorganization, as Judge Anderson found (A513-514), Manufacturers suggests two more concepts: (1) that only a conflict of "legal positions" was involved (Manu. Br. 17) and (2) that "[a]bsent use of confidential information or overreaching, once a trustee has resigned from a trust, his fiduciary obligations to the trust cease and he may thereafter deal with his former cestuis in the normal course of business." (Manu. Br. 19, n. 17)(Emphasis added). Neither justifies payment to Manufacturers while in its conflict.

As to the first point, surely, an attorney could not represent two clients on opposite sides of a lawsuit in which the only issues involved are questions of law, even though the facts are undisputed. To say, as Manufacturers does, that the representation of conflicting legal interests is permissible so long as other parties in interest are involved on both sides of the dispute (Manu. Br. 17), and that it really doesn't matter what counsel advocates in litigation, since counsel is in no way responsible for "the judicial action of this Court" (Manu. Br. 18), ignores the fundamental premise that only a disinterested fiduciary is entitled to compensation.[9]

9. If Manufacturers' assertion to this Court that its control of its conflicting lawyers "consisted simply of authorizing its counsel for each interest to fight as hard as they could for the position of their cestuis" (Manu. Br. 17, n. 15) were factually accurate, it would demonstrate an additional breach of trust by Manufacturers: a breach of its duty not to delegate to others the doing of acts which it should perform itself. A trustee "can properly consult with and take advice from others provided he personally makes the final decision in the matter." Restatement (Second) of Trusts §171, comment f (1959)(Emphasis added). The impropriety of the device of hiring separate counsel, and of the "insulation" theory, is highlighted by the fact that by taking such actions Manufacturers created a situation in which it was inevitable that it would either breach its duty of loyalty to one of its cestuis by making a decision with regard to the equitable lien litigation, or that it would breach its duty not to delegate by avoiding all decision-making.

As to the second point, the authorities relied on by Manufacturers for this proposition--II Scott on Trusts §170.8 (3d Ed. 1967); Restatement (Second) of Trusts §170, comment g (1959) (Manu. Br. 19, n. 17)--state only that a former trustee, after the termination of the trust, is under no absolute prohibition from purchasing trust property. Manifestly that factual situation is not involved here. Moreover, a fiduciary's duty of loyalty to a former cestui is not solely limited to situations involving overreaching or breach of confidence. In particular, where a fiduciary represents parties whose interests become adverse--the factual situation in this case--the duty of loyalty demands that he either apply to the court for instructions or resign from both positions, rather than adhere to one and attack the other, as Manufacturers is doing here. Restatement (Second) of Trusts §170, comment r (1959); H. Drinker, Legal Ethics 104-112 (1953).

In the case at bar, then, Manufacturers is not "disinterested," served "more than one master" and "has an actual conflict of interest," within the meaning of Woods. 312 U.S. at 269. Certainly no more need be shown to revoke the payment to this former indenture trustee.[10]

10. Manufacturers would have this Court ignore Woods' command that a tainted fiduciary "should be denied compensation," 312 U.S. at 268, because in Securities and Exchange Commission v. Chenery Corp., 318 U.S. 80, 89 (1943), the Supreme Court characterized Woods as holding that a bankruptcy court "could" deny compensation (Manu. Br. 21-22). But this use of the word "could," in dictum, in a case involving not compensation to fiduciaries in a bankruptcy situation but rather the S.E.C.'s approval of a reorganization plan under the Public Utilities Holding Company Act, 15 U.S.C. §79 et seq., cannot serve to change the essence of the Woods rule, as reaffirmed--after Chenery--in Wolf. In pressing this argument, Manufacturers ignores this Court's warnings "against the literal application of language in Supreme Court opinions to different factual situations." Local 1104, Communications Workers of America, AFL-CIO v. National Labor Relations Board, 520 F.2d 411, 416 (2 Cir. 1975), cert. denied, 423 U.S. 1051 (1976).

III. THE NEW HAVEN TRUSTEE AND HIS CHANGE OF HEART.

Trustee Smith's position with respect to the conflict of interest of Manufacturers has undergone an amazing metamorphosis since the matter was before the Reorganization Court: conduct which he there described as "wrong on any standard of morality that's above that of the common marketplace" (A556-557) with respect to the issue which "is of utmost significance to every creditor of the Estate (with the possible exception of the highest priority administration claimants)," (A292), he now describes before this Court as a "technical" conflict without proof of damage (Smith Br. 10-12). Not once, in the Court below, did the New Haven trustee use the word "technical" to describe the conflict (A270-322); here he does so on no less than eight occasions (Smith Br. 1-25).

The Reorganization Trustee bases no specific argument on the repeated reference to the word "technical". Insofar as he suggests by the mere use of the term that there should be a tolerance of the type of conflict here involved, the trustee offers no legal authority to buttress such a position. And, indeed, it would be difficult to find such authority for, as Mr. Justice Cardozo wrote for the New York Court of Appeals in the landmark decision to which the New Haven trustee apparently made reference in the court below:

> "Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions....Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd." Meinhard v. Salmon, et al, 249 N.Y. 458, 164 N.E. 545, 546 (1928).

Moreover, the Reorganization Trustee challenges a specific finding of the Reorganization Court. In emphasizing that there was no "proof of damage" (Smith Br. 10-14), the trustee ignores Judge Anderson's finding that Manufacturers "impeded, and therefore, damaged, the New Haven reorganization trustee's collection of sums owed the New Haven estate..." (A514). To be sure, at Manufacturers' request, Judge Anderson clarified this finding with regard to damage to emphasize what was obvious: that only the issue of compensation--not an action for damages--was before him when he issued his opinion (A577). But Judge Anderson in no way retreated from his position that, with respect to the compensation issue now before this Court, Manufacturers had damaged the estate (A577).

The trustee also argued that Manufacturers "contributed substantially to the increased price" for the New Haven assets and "thereby benefited the Estate" for which it was "entitled to substantial compensation." (Smith Br. 6). What is ignored is that Judge Anderson, as noted, specifically found that Manufacturers attempted to block effective collection of the price--both the original and increased price--of those assets (A513-514). It is difficult to comprehend how Manufacturers' effort to increase the price of the assets and then prevent the payment to the New Haven estate of that price can be a benefit to the New Haven estate.

Even as the Reorganization Trustee refers to the conflict as "technical" in his effort to permit the payment of up to $1,535,568.83 to the former indenture trustee which "impeded" (A514) the reorganization, he recognizes that Manufacturers' conflict dealt with

"matters vital to the New Haven Estate." (Smith Br. 13) and concedes:

> "Messrs. Iannotti and Zeldes correctly state that the insulation theory was approved neither by the New Haven Reorganization Court nor by the Penn Central Reorganization Court. (A391). Manufacturers never petitioned either the New Haven Reorganization Court or the Penn Central Reorganization Court with regard to the appointment of a guardian ad litem, substitute trustee, or, for that matter, any advice or instructions concerning its conflicting situation. (A387-390)" (Smith Br. 11).

Conclusion

Although it takes issue with some statements of the Successor Trustees, Manufacturers in its brief leaves unchallenged these assertions:

--that Simpson, Thacher and Bartlett and Kelley Drye, both representing Manufacturers, took opposite sides on the equitable lien issue before this Reorganization Court;

--that after Manufacturers resigned from its New Haven trusteeship it opposed, through the efforts of Kelley Drye, the New Haven estate's interests on the equitable lien issue both before this Court and the Supreme Court;

--that the "insulation theory" was knowingly adopted by Manufacturers on the advice of both Simpson, Thacher and Bartlett and Kelley Drye but without any court approval;

--that indeed no petition for instructions was filed with any court upon the ripening of the conflict;

--that Manufacturers remained in a position of conflict despite its chairman's admonition to resign from both sides;

--that its opposing counsel--Simpson, Thacher and Bartlett and Kelley Drye--reported to the same official at Manufacturers;

--that Manufacturers is now hostile to the New Haven estate by virtue of its remaining trusteeships and by virtue of its status as creditor of the Penn Central (A29, 94-95);

--that in this hostile posture Manufacturers has taken, and considers itself to have a duty to take in the future, positions adverse to the interests of the New Haven;

--that Manufacturers will pay Simpson, Thacher and Bartlett regardless of this Court's decision on this appeal; and

--that Manufacturers does not object to the imposition by the Reorganization Court of some penalty, in form of a contingent payment of its fee, as a result of its conflict of interest.

This unchallenged record warrants a reversal of the Reorganization Court's judgment.

For these reasons, then, that portion of the judgment of the court below which granted Manufacturers' petition for payment for services and expenses should be--and the Successor Trustees respectfully request that it be--reversed.

Dated at Bridgeport, Connecticut, this 30th day of December, 1976.

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IN THE DISTRICT COURT OF THE UNITED STATES
FOR THE DISTRICT OF CONNECTICUT

SEP 25 1961

In the Matter of THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, Debtor.	In the Proceedings for the Reorganization of a Railroad No. 30226

ORDER PERMITTING INTERVENTION OF MANUFACTURERS TRUST COMPANY, CORPORATE TRUSTEE AND A. FREDERICK KOUTHEN, SUCCESSOR INDIVIDUAL TRUSTEE, UNDER FIRST AND REFUNDING MORTGAGE DATED AS OF JULY 1, 1927 OF THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY

On this day coming on to be heard the petition verified July 25, 1961 of Manufacturers Trust Company, Corporate Trustee, and A. Frederick Kouthen, Successor Individual Trustee, under the Debtor's First and Refunding Mortgage dated as of July 1, 1927 for leave to intervene with proof of service on the attorney for the Debtor and all other parties to the proceeding; and, for good cause shown, the Court, being duly advised in the premises, finds that the petition should be granted, that the facts set forth in said petition do not constitute a conflict of interest on the part of the petitioners which would make it inappropriate for them to participate in this proceeding on behalf of the holders of the Debtor's First and Refunding Mortgage Bonds, 4½, Series A, or which would affect their rights, and the rights of their counsel, hereafter to make application to the Court for and obtain compensation for services rendered and reimbursement of expenses incurred in connection with or during this proceeding, and that the petitioners should be allowed to intervene herein, it is therefore ORDERED:

1. That Manufacturers Trust Company, Corporate Trustee, and A. Frederick Keuthen, Successor Individual Trustee, of the Debtor's First and Refunding Mortgage dated as of July 1, 1947 be permitted to intervene generally herein and be admitted and constituted as general parties to these proceedings, for the purpose of protecting their rights and the rights of the holders of the Bonds secured by said Mortgage.

2. That the Court reserves the right, without notice to said Corporate Trustee and said Successor Individual Trustee, to enter orders relative to administration of the proceedings and the operation of the property being administered by the Court in these proceedings, including the property covered by the lien of said Mortgage, which do not disturb the lien of said Mortgage.

E N T E R.

District Judge

Dated: September 6th, 1961

DOCKET NO. 76-5025,
76,5030,
76,5033,
76-5037-8

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In the Matter of The New York, New Haven and Hartford Railroad Company, Debtor

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LAWRENCE W. IANNOTTI, Successor Indenture Trustee Under The New York, New Haven And Hartford Railroad Company's First And Refunding Mortgage Dated As Of July 1, 1947; and

JACOB D. ZELDES, Successor Indenture Trustee Under The New York, New Haven And Hartford Railroad Company's General Income Mortgage Dated As Of July 1, 1947,

Appellants

v.

MANUFACTURERS HANOVER TRUST COMPANY, Former Indenture Trustee Under The New York, New Haven And Hartford Railroad Company's First And Refunding Mortgage Dated As Of July 1, 1947; and

RICHARD JOYCE SMITH, Trustee Of The Property Of The New York, New Haven And Hartford Railroad Company, Debtor,

Appellees

CERTIFICATE OF SERVICE

I, Jacob D. Zeldes, Successor Indenture Trustee Under The New York, New Haven And Hartford Railroad Company's General Income Mortgage Dated As Of July 1, 1947, in the above-entitled matter, hereby certify that on the 30th day of December, 1976, I served the attached Reply Brief of Successor Indenture Trustees upon attorneys for appellees and other parties in interest by depositing copies in the U.S. mails, postage prepaid, addressed to them at the following addresses:

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Dated at Bridgeport, Connecticut this 30th day of December, 1976.

Jacob D. Zelden